Guinness Atkinson

China & Hong Kong Fund

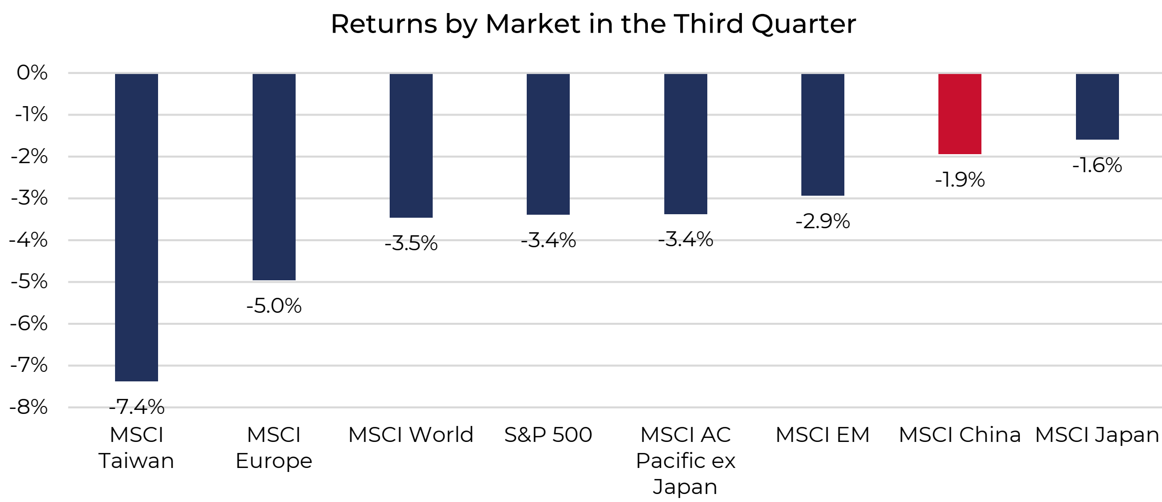
Managers' Update – Review of September 2023

Summary View

- The best performing stocks in the Fund in the quarter were Suofeiya Home Collection, Netease and Alibaba.
- The weakest stocks in the Fund in the quarter were Xinyi Solar, Wuxi Lead Intelligent Equipment and Hangzhou First Applied Material.
- The Fund is trading on a forward year price earnings ratio of 13.6x. The current set of holdings is trading at one of the lowest levels seen in the past decade.
- Over the past 10 years, our holdings have in aggregate grown earnings by 8% a year. Based on consensus analyst estimates, the Fund is expected to grow earnings by 20% a year over the next two years.

Market Commentary

(Performance data in the section in USD terms unless otherwise stated)

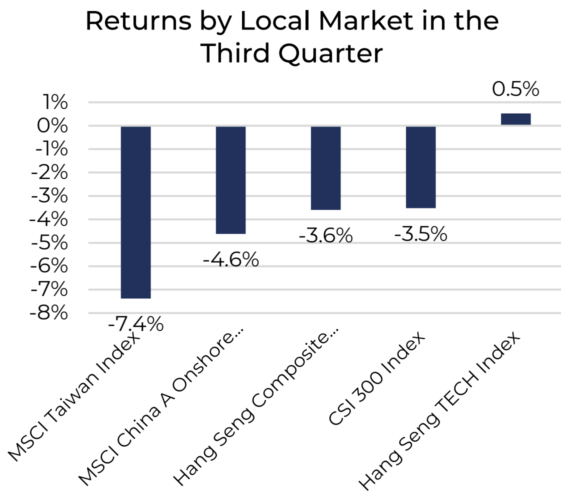


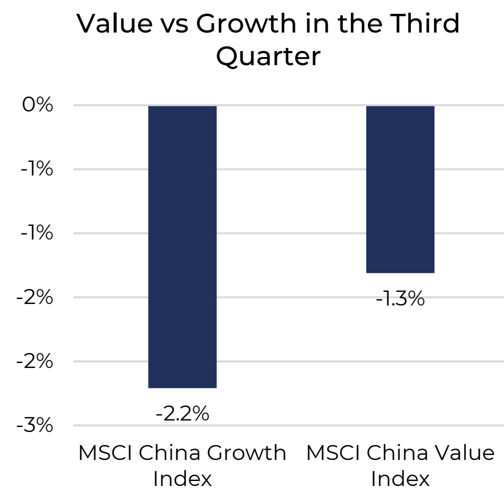
(Data from 06/30/23 to 09/30/23, returns in USD, source: Bloomberg, Guinness Atkinson calculations)

In the third quarter, the MSCI China Index fell by 1.9%. This compared to the 3.5% fall seen for the MSCI World Index.

In July, Chinese markets rallied with the MSCI China Index rising by 10.8%. Markets were strong on expectations of greater stimulus for the housing market and wider economy. The readout from the Politburo's meeting acknowledged "insufficient domestic demand" and mentioned the need for counter-cyclical economic policy. Supporting the private sector was mentioned, though at the time we argued actions rather than rhetoric was needed. The phrase "housing is for living, not for speculation" was removed from the statement, which was interpreted by most as a sign that more easing measures for the property market were on the way. Though we do point the phrase later reappeared in other government documents, indicating the government is unlikely to unleash another property bubble.

The gains were erased over the next two months as the MSCI China Index fell by 9.0% in August and a further 2.8% in September. Wealth management products run by Zhongrong Trust failed to repay lenders, leading to fears over the strength of China's broader financial system. Country Garden, a large private property developer, failed to repay its maturing bonds on time. We also saw the ramp up in the anti-corruption campaign in the healthcare sector.

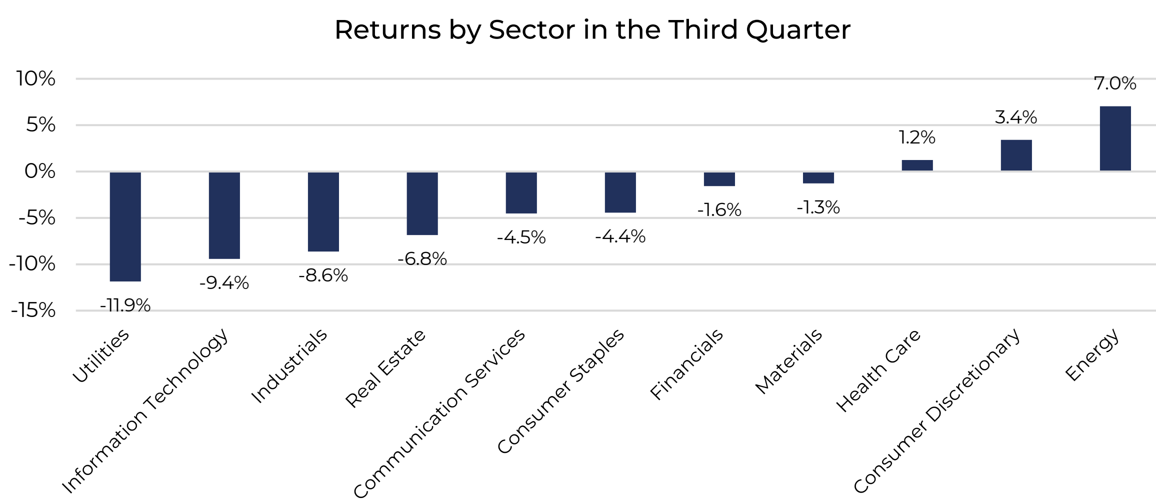




(Data from 06/30/23 to 09/30/23, returns in USD, source: Bloomberg, Guinness Atkinson calculations)

Onshore and offshore China equity markets behaved similarly in the third quarter. Offshore markets, as measured by the Hang Seng Composite Index, fell by 3.6%. Onshore markets, as measured by the MSCI China A Onshore Index, fell by 4.6%.

Growth stocks underperformed slightly as the MSCI China Growth Index fell by 2.2%, compared to the MSCI China Value Index which fell by 1.3%.

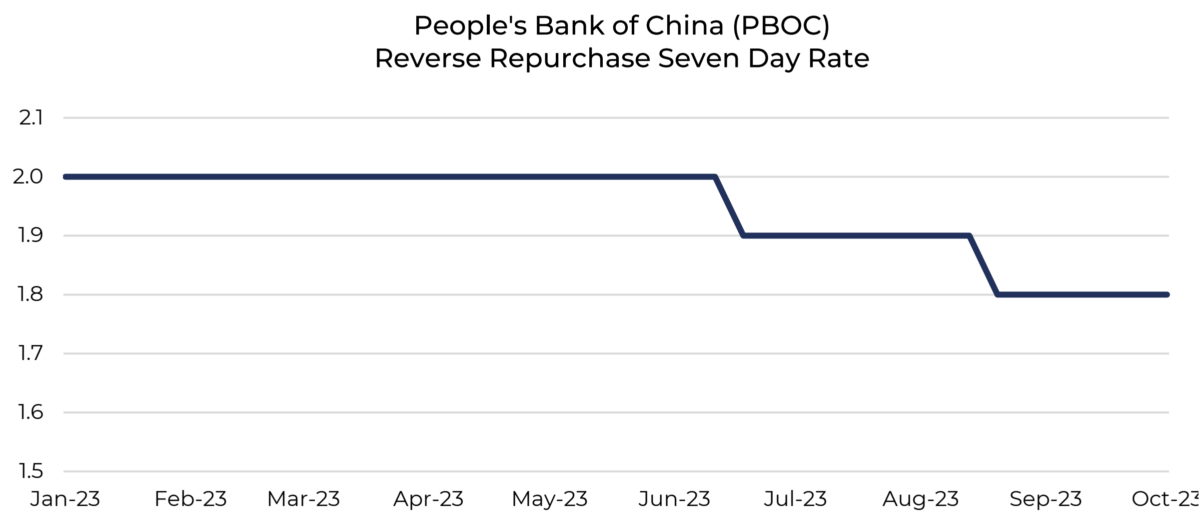


(Data from 06/30/23 to 09/30/23, returns in USD, source: Bloomberg, Guinness Atkinson calculations)

In the third quarter, the best performing sectors were Energy (total return +7.0%), Consumer Discretionary (+3.4%) and Health Care (+1.2%). Rising oil prices and good results led to strength for the Energy sector. In the Consumer Discretionary Sector, companies such as Pinduoduo and Xpeng were outperformers. Though affected by the ongoing anti-corruption campaign, the biotech names within Healthcare outperformed.

The weakest sectors were Utilities (total return -11.9%), Information Technology (-9.4%) and Industrials (-8.6%). Within Utilities, the gas distributors were weakest. Within Information Technology, the weakest names were related companies in the solar supply chain: Xinyi Solar, GCL Technology, Daqo New Energy and Flat Glass. Falling module prices and possible overcapacity led to weakness across various companies in the supply chain.

Macro Stimulus

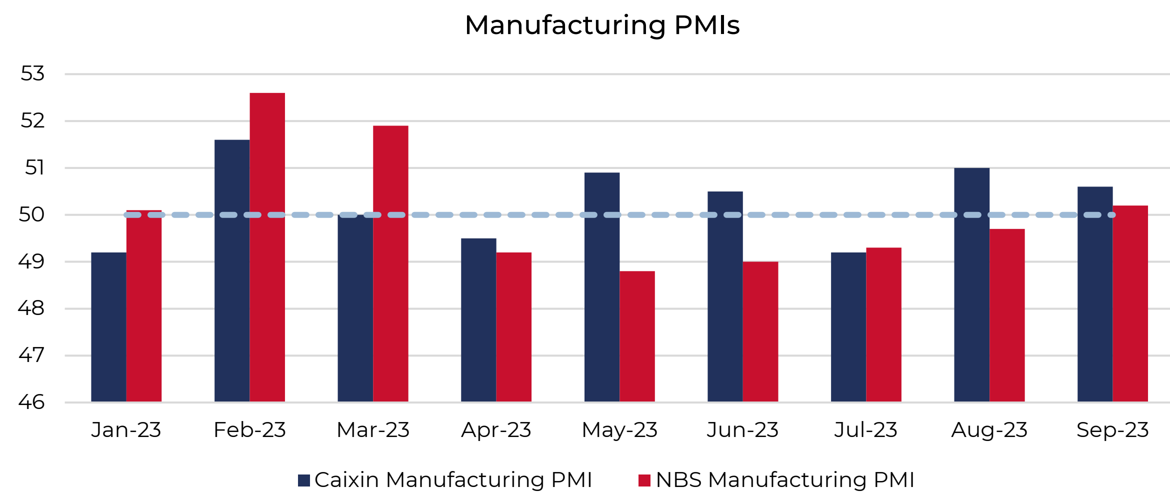


(Data from 12/31/22 to 09/30/23, source: Bloomberg, Guinness Atkinson calculations)

Since June, the government has twice cut short-term interest rates, which in China we refer to the seven-day reverse repurchase (repo) rate. In June the seven-day repo rate was cut from 2.0% to 1.9%; in August rates were cut further to 1.8%.

Over the summer, we have seen clear signs of stimulus to boost both the housing market and the overall economy.

- The definition of a first home has been relaxed, so more households are eligible for cheaper mortgages, which should practically benefit the tier one cities.
- Minimum mortgage rates for second homes have been cut from 0.6% above the five-year loan prime rate (LPR) to 0.2% above the five-year LPR. In essence, this is a further cut to mortgage rates on top of the 0.2% reduction in the five-year LPR year-to-date.
- Importantly, banks are being told to apply these new lower bounds to existing mortgage holders who are refinancing.
- Required reserve ratios have been cut, from 7.8% in Dec-22 to 7.6% in June and now 7.4% in September.
- Tax deductions have been increased for childcare and elderly care, which should lead to higher disposable incomes.



(Data from 01/31/23 to 09/30/23, source: Bloomberg, Guinness Atkinson calculations)

China's macroeconomic data points were weak over the spring and much of summer, but we are seeing incrementally better data. High frequency data points such as the manufacturing Purchasing Managers' Index illustrate the point, where a number above 50 indicates expanding activity and a number below 50 indicates weakening activity. The Caixin Manufacturing PMI, which is more geared towards private enterprises, recovered from 49.2 in July to 51.0 in August, before moderating to 50.6 in September which still indicates healthy activity. The National Bureau of Statistics (NBS) PMI, which is more geared towards state owned enterprises (SOEs), recovered from 49.3 in July to 49.7 in August and 50.2 in September.

Fund Commentary

The strongest stocks in the portfolio were:

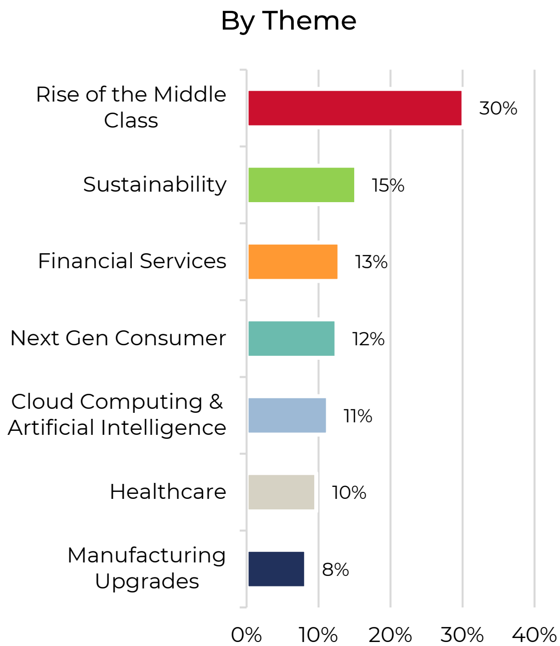
- Suofeiya Home Collection (total return +8%) – in the first half of 2023, revenue fell 1% and earinings per share (EPS) rose 21%. Suofeiya is a manufacturer of wardrobes and kitchen cabinets. The company has reduced its direct exposure to property developers, with their sales contribution falling from a peak of 18% a few years ago to 12% in the second quarter of this year.
- Netease (total return +4%) – the business' Eggy Party game is performing very well, reaching 100 million monthly active users in August. For context, China has 660 million gamers so the game is a huge success. While Netease is mostly known for its games targeting hardcore gamers, Eggy Party targets the casual gamer and is the most downloaded game in China this year. The company's other recent release, Justice Mobile, is also targeting new users and earned RMB 5 bn (Renminbi) in its first two months of release.
- Alibaba (total return +4%) – Alibaba reported better than expected quarterly results which has led to positive earnings revisions. Sales in the core e-commerce business grew 10% while revenues from the cloud segment grew 4%. The business has been reorganized into six business groups, some of which may pursue a public listing. This reorganization should allow each group to better grow in their particular markets.

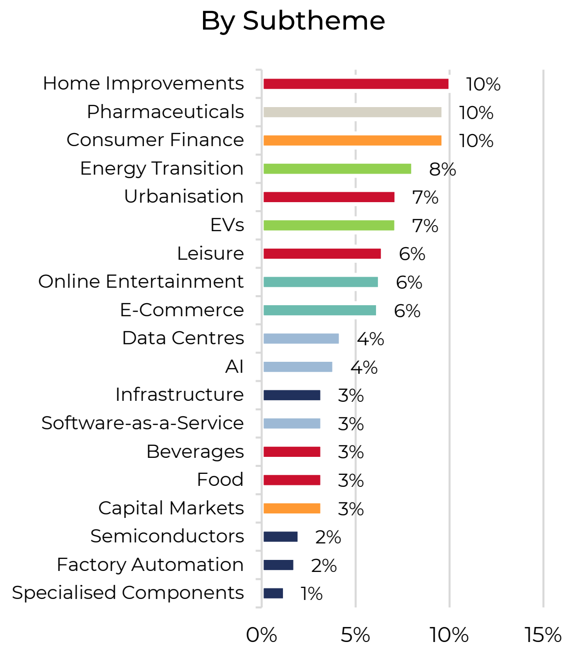
The weakest stocks in the portfolio were:

- Xinyi Solar (total return -35% in the third quarter) – in the first half of 2023, revenue rose 25% and EPS fell 27%. Xinyi Solar is the world's largest manufacturer of solar glass. In its interim results the company reported year-on-year volume growth of 50%, revenue growth of 25% but a net income contraction of 27%. Volume growth was strong as demand for solar energy continues to grow both domestically and abroad. Revenue growth of 25% is attractive in the current macro environment, but lagged volume growth as greater solar glass capacity within the industry led to lower selling prices. The company's gross margin fell by 8.7% percentage points. Natural gas and soda ash prices remained elevated in the first quarter, but the company did not benefit from falling raw material prices in the second quarter. This is because it signed natural gas contracts at the end of last year at fixed prices, when concerns over gas shortages were at their highest. In the second half of the year, management expect to benefit from cheaper gas prices as the contracts roll over. Despite the results, Xinyi Solar is continuing to add capacity in order to gain market share. As the lowest-cost producer in the space with a strong balance sheet, the company is in a good position to take advantage where its smaller competitors are struggling. We expect the supply-demand imbalance to gradually adjust, as smaller peers are unlikely to be able to afford expansion, putting Xinyi Solar in a favorable position.
- Wuxi Lead Intelligent Equipment (total return -25%) – in the first half of 2023, revenue grew 30% and EPS grew 48%. Lead Intelligent is a manufacturer of battery production equipment, whose second largest shareholder is CATL, one of the world's largest battery manufacturers. Given potential overcapacity in China, export growth is likely to be important for Lead Intelligent. Therefore, it was good to see the business sign up LG Energy Solutions, the first major Korean customer that Lead Intelligent has worked with. Automotive Cells Company (a joint venture operated between Mercedez-Benz Group, Stellantis and Total Energies) is Lead Intelligent's second largest foreign customer. Volkswagen and Northvolt are other major clients that Lead Intelligent supplies.
- Hangzhou First Applied Material (total return -24%) – in the first half of 2023, revenue grew 18% but EPS fell 26%. First Applied Material is the world's largest manufacturer of solar film, which is used to protect solar modules. The company's volume of solar film shipped increased by 57% in the interim period, but average selling prices fell 25%, reflecting lower prices across the industry. First Applied Material used up most of its higher cost inventory in the first quarter and is now expecting higher prices going forward. The business increased prices in August and to secure lower input costs, has made prepayments to its suppliers. This is expected to lead to higher margins.

Portfolio Positioning

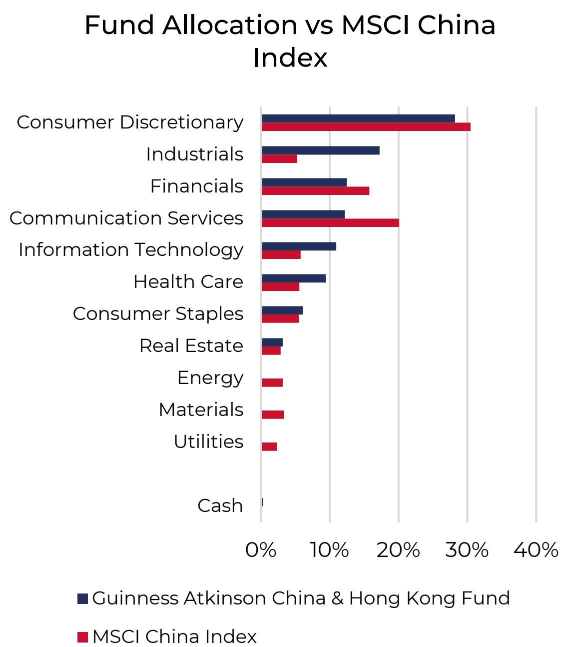
By theme, the Fund's largest exposures are to the Rise of the Middle Class, followed by Sustainability and Financial Services. Important subthemes include Home Improvements, Pharmaceuticals and Consumer Finance.

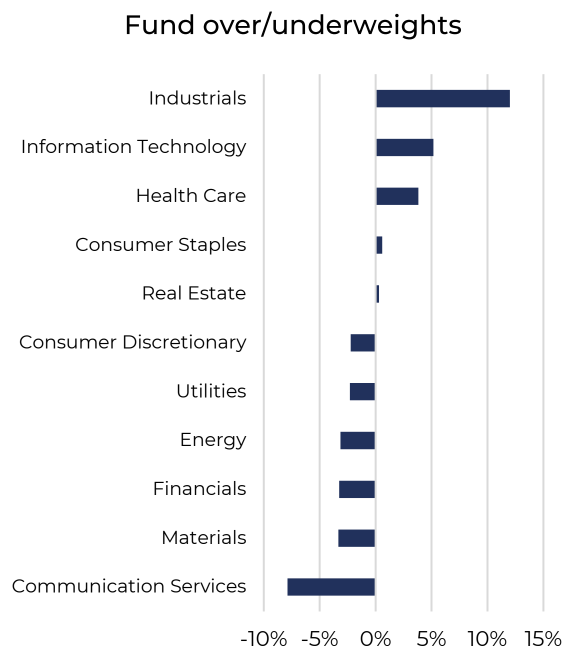




(Data as of 09/30/23, source: Guinness Atkinson calculations)

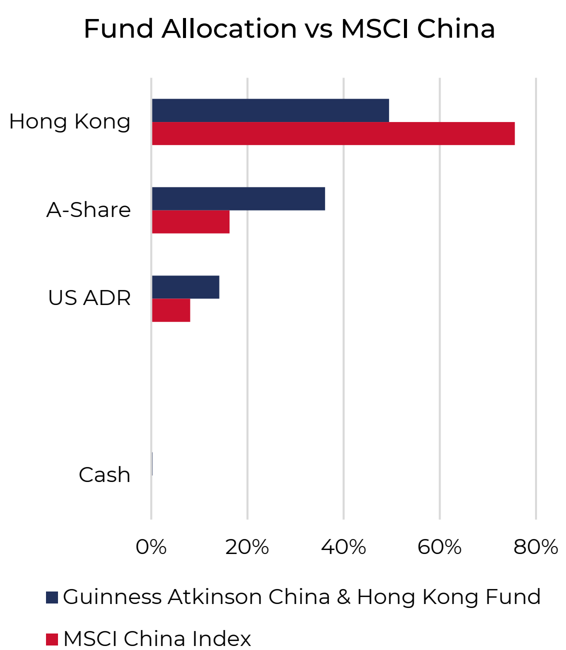
On a sector basis, the Fund's largest exposures are to Consumer Discretionary and Industrials. The Fund has no exposure to Utilities, Energy or Materials. Relative to the MSCI China Index, the Fund is overweight in Industrials and Information Technology. The Fund is underweight in Communication Services.

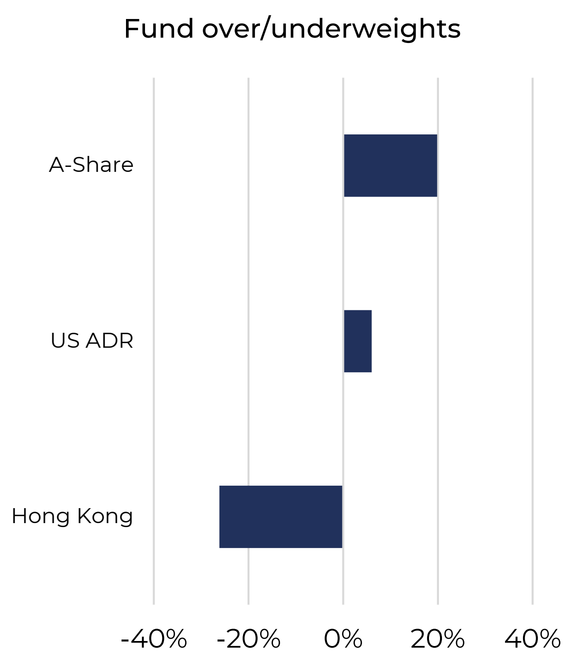




(Data as of 09/30/23. Source: Bloomberg, MSCI, Guinness Atkinson calculations)

On a listing basis, the Fund has 49% exposure to stocks listed in Hong Kong and 36% exposure to the A share market. 14% of the Fund is also held in Chinese companies trading on US exchanges (Alibaba, JD.com, Netease and Baidu).





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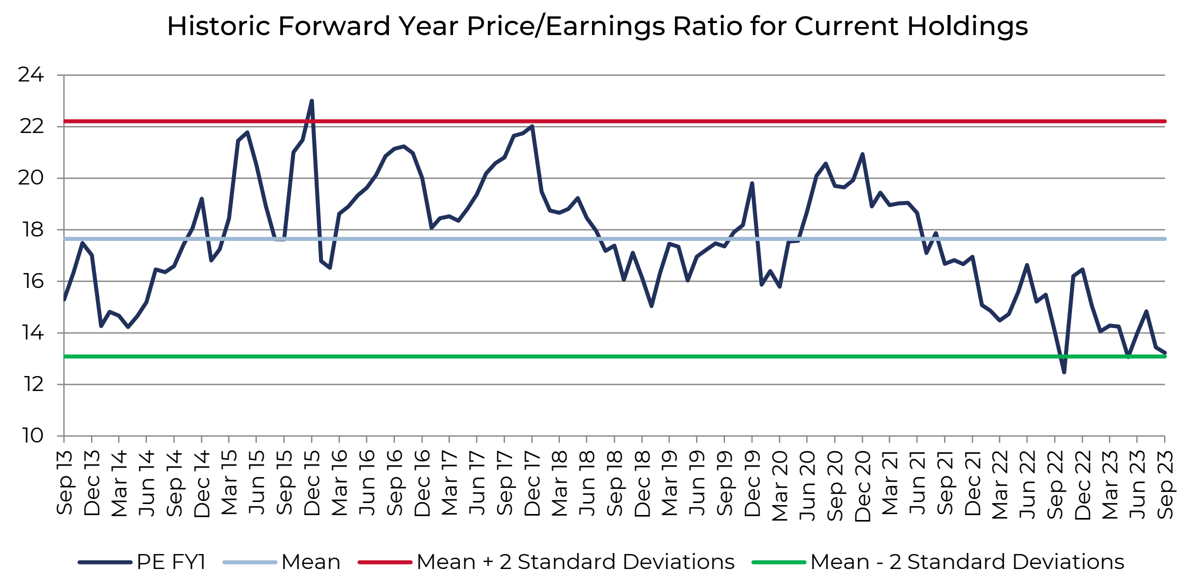
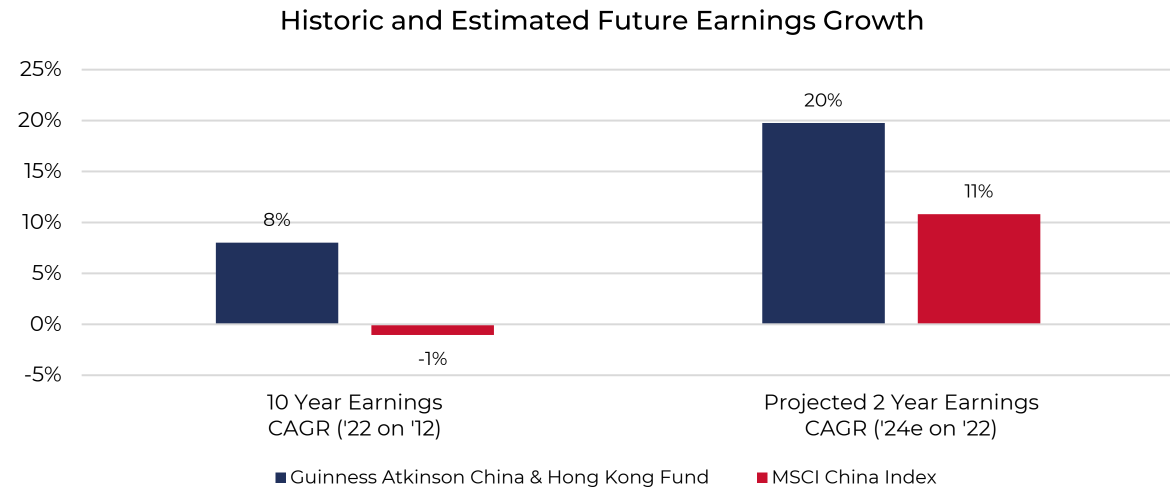
Outlook



(Data from 09/30/13 to 09/30/23, source: Bloomberg, Guinness Atkinson calculations)

We argue that talk of the collapse of China's financial system is unwarranted. Markets are to an extent pricing in this scenario, whereas we argue China has the capital in place in the banking system to absorb losses arising from the property market and wider economy. Therefore, if markets are pricing in a scenario which we have assessed as unlikely, then this is an opportunity for investors. The Fund is trading on a forward year price earnings ratio of 13.6x which is close to two standard deviations below the current' holdings 10-year historic average. This valuation does not appear often for the high quality, compounding stocks we hold in the Fund. Over the past decade, our holdings in aggregate have grown earnings by 8% a year. Based on consensus analyst estimates, the Fund's holdings in aggregate are expected to grow earnings by 20% a year over the next two years.



(Source: Bloomberg, MSCI, Guinness calculations. Data as of 09/30/2023. Sales in USD Fund series assumes $1m equally weighted into current holdings. Data for the Fund is a simulation based on actual, aggregate, historic data for the Funds' current holdings. Index data uses historic holdings as of the end of each year)

Edmund Harriss (portfolio manager)

Sharukh Malik (portfolio manager)

Performance

Relative to MSCI China Index, areas which helped the Fund's performance in the quarter were:

- Stock selection, driven by Suofeiya Home Collection, Netease and Alibaba.
- Stock selection in Real Estate. The only property developer we hold is China Overseas Land & Investment, which is a conservatively financed developer that has been active in acquiring projects while private developers have pulled back. Its share price has outperformed the sector.
- Underweight to Tencent. The Fund is run on an equally weighted basis and so each stock has a neutral weight of ~3.2%. As of Aug-23, Tencent had a weight of 13.1% in the MSCI China Index. Therefore, when Tencent underperforms, the Fund captures less of the downside than the broader market.
- Underweight to Utilities, where the Fund holds no utilities.

Areas which detracted from the Fund's relative performance were:

- Weakness in the solar related companies: Xinyi Solar and Hangzhou First Applied Material. Additionally, we saw weakness in some of our electric vehicle exposure through Wuxi Lead Intelligent.
- Healthcare sector exposure: Sino Biopharmaceutical, China Medical System and CSPC Pharmaceutical. The three are pharmaceutical companies making the transition away from generic drugs towards innovative drugs. The sector is being affected by the anti-corruption push, which is leading to a slowdown in sales that is expected to last for another quarter or two. We estimate at current valuations, the market is assigning zero value to the cashflows generated from future capital expenditures and R&D. We believe there is a strong chance these companies will eventually make their own innovative drugs, and so at current prices these companies are a bargain.
- Underweight to Pinduoduo. We do not own the stock because of its poor track record of converting revenue growth into cashflow growth. We also think management is not transparent with shareholders in its disclosures.
- Not holding the large state-owned banks, which benefited from value stocks' outperformance. The Fund's only bank holding is China Merchants Bank.

As of 09/30/2023	YTD	1 Year	3 Year	5 Year	10 Year
China & Hong Kong Fund (ICHKX)	-12.46%	-0.08%	-10.25%	-3.91%	0.84%
Hang Seng Composite Index TR	-7.18%	8.85%	-7.61%	-3.57%	1.57%
MSCI China Net Total Return Index	-7.29%	5.24%	-14.28%	-4.16%	1.67%

All returns over 1 year annualized. *Source: Bloomberg, Guinness Atkinson Asset Management.*

Expense Ratio: 1.71%

Performance data quoted represents past performance; past performance does not guarantee future results. The investment return and principal value of an investment will fluctuate so that an investor's shares, when redeemed, may be worth more or less than their original cost. Current performance of the Fund may be lower or higher than the performance quoted. Performance data shown is current to the most recent month and quarter end. To obtain performance as of the most recent month end, please visit www.gafunds.com or call 1-800-915-6565. Performance data does not reflect the 2% redemption fee for shares held less than 30 days and, if deducted the fee would reduce the performance noted.

The Fund's investment objectives, risks, charges and expenses must be considered carefully before investing. The statutory and summary prospectus contains this and other important information about the investment company, and it may be obtained by calling 800-915-6566 or visiting gafunds.com. Read it carefully before investing.

Investments in foreign securities involve greater volatility, political, economic and currency risks and differences in accounting methods. These risks are greater for emerging markets countries. The China and/or Hong Kong stock markets in which the Fund invests may experience periods of volatility and instability. These fluctuations may cause a security to be worth less than it was at the time of purchase. Market risk applies to individual securities, a particular sector or the entire economy. China and/or Hong Kong stocks may fall out of favor with investors, the value of Chinese currencies may decline relative to the U.S. dollar and/or China or Hong Kong stock markets may decline generally. The Fund invests in invest in small-cap or mid-cap, which involve additional risks such as limited liquidity and greater volatility, than investments in larger companies.

One cannot invest directly in an Index.

The People's Bank of China (PBOC) is the central bank of the People's Republic of China, responsible for carrying out monetary policy and regulation of financial institutions in China, as determined by the People's Bank Law and the Commercial Bank Law.

P/E ratio is a current stock price over its earnings per share. The forward P/E ratio is a current stock's price over its "predicted" earnings per share. If the forward P/E ratio is higher than the current P/E ratio, it indicates decreased expected earnings.

Standard deviation is a statistic that measures the dispersion of a dataset relative to its mean and is calculated as the square root of the variance. If the data points are further from the mean, there is a higher deviation within the data set. A volatile stock has a high standard deviation, while the deviation of a stable blue-chip stock is usually rather low.

The compound annual growth rate (CAGR) is the rate of return (RoR) that would be required for an investment to grow from its beginning balance to its ending balance, assuming the profits were reinvested at the end of each period of the investment's life span.

The Producer Price Index (PPI) program measures the average change over time in the selling prices received by domestic producers for their output. The prices included in the PPI are from the first commercial transaction for many products and some services.

The Consumer Price Index (CPI) is a measure of the average change over time in the prices paid by urban consumers for a market basket of consumer goods and services. Indexes are available for the U.S. and various geographic areas. Average price data for select utility, automotive fuel, and food items are also available.

USD/CNY is the abbreviation for the US Dollar and Chinese Yuan pair. It shows how much the USD (base currency) is worth as measured against the CNY (counter currency).

The MSCI China A Onshore Index captures large and mid cap representation across China securities listed on the Shanghai and Shenzhen exchanges.

The Shanghai Shenzhen CSI 300 Index is a market capitalization-weighted stock market index designed to replicate the performance of the top 300 A-share stocks traded in the Shanghai and Shenzhen stock exchanges.

Hang Seng Composite Total Return Index is a market capitalization weighted index that monitors the performance of stocks listed in Hong Kong.

In China, the National Bureau of Statistics (NBS) Manufacturing Purchasing Manager Index measures the performance of the manufacturing sector and is derived from a survey of more large-scale, state-owned companies. The Manufacturing Purchasing Managers Index is based on five individual indexes with the following weights: New Orders (30%), Output (25%), Employment (20%), Suppliers' Delivery Times (15%) and Stock of Items Purchased (10%), with the Delivery Times index inverted so that it moves in a comparable direction.

The Basel Accords are a series of three sequential banking regulation agreements (Basel I, II, and III) set by the Basel Committee on Bank Supervision (BCBS). Basel III is an international regulatory accord that introduced a set of reforms designed to mitigate risk within the international banking sector by requiring banks to maintain certain leverage ratios and keep certain levels of reserve capital on hand. Basel III is an internationally agreed set of measures developed in response to the financial crisis of 2007-2009.

A nonperforming loan (NPL) is a loan that is in default due to the fact that the borrower has not made the scheduled payments for a specified period.

The Caixin PMI measures the performance of the manufacturing sector and is derived from a survey of more private companies.

MSCI AC Asia Pacific ex Japan Index is free float-adjusted market capitalization weighted index that is designed to measure the equity market performance of countries in the Asia Pacific region.

MSCI Europe Index is a free float-adjusted market capitalization weighted index that is designed to measure the equity market performance of European markets.

MSCI EM Index is a free float-adjusted market capitalization weighted index that is designed to measure the equity market performance of Emerging markets in Asia, Europe, Middle East, Africa and Latin America.

MSCI China Index captures large and mid cap representation across China A shares, H shares, B shares, Red chips, P chips and foreign listings (e.g. ADRs). With 703 constituents, the index covers about 85% of this China equity universe.

The MSCI China A Index captures large and mid-cap representation across China securities listed on the Shanghai and Shenzhen exchanges. The index is designed for international investors and is calculated using China A Stock Connect listings based on the offshore RMB exchange rate (CNH)

MSCI Hong Kong Index is a capital weighted stock index designed to measure the performance of the large and mid cap segments of the Hong Kong market. It has 48 constituents and covers approximately 85% of the free float-adjusted market capitalization of Hong Kong equity stocks.

MSCI Japan Index is a free float-adjusted market capitalization weighted index that is designed to measure the equity market performance of the Japanese market.

MSCI World Index is a free float-adjusted market capitalization weighted index that is designed to measure the equity market performance of developed markets.

MSCI China Growth Index captures large and mid cap securities exhibiting overall growth style characteristics across the Chinese equity markets.

MSCI China Value Index captures large and mid cap Chinese securities exhibiting overall value style characteristics. The value investment style characteristics for index construction are defined using three variables: book value to price, 12-month forward earnings to price, and dividend yield.

S&P 500 Index is a market-capitalization-weighted index of leading publicly traded companies in the U.S.

The Hang Seng Composite Index ("HSCI") offers a comprehensive Hong Kong market benchmark that covers about the top 95th percentile of the total market capitalisation of companies listed on the Main Board of the Stock Exchange of Hong Kong ("SEHK").

Hang Seng TECH Index represents the 30 largest technology companies listed in Hong Kong that have high business exposure to technology themes and pass the index's screening criteria.

The MSCI Taiwan Index is designed to measure the performance of the large and mid cap segments of the Taiwan market. With 90 constituents, the index covers approximately 85% of the free float-adjusted market capitalization in Taiwan.

Privately owned enterprise (POE) is a business that is managed by an independent company or private individual — rather than the Chinese Government or the host country government. While these companies may issue stock and have shareholders, their shares are not listed on public exchanges.

American depositary receipt (ADR) refers to a negotiable certificate issued by a U.S. depositary bank representing a specified number of shares—usually one share—of a foreign company's stock. The ADR trades on U.S. stock markets as any domestic shares would.

Earnings per share (EPS) is calculated as a company's profit divided by the outstanding shares of its common stock.

The Renminbi(RMB) is the official name of China's currency. The principal unit of RMB is called the Chinese Yuan (CNY).

Many investors use the price-to-book ratio (P/B ratio) to compare a firm's market capitalization to its book value and locate undervalued companies. This ratio is calculated by dividing the company's current stock price per share by its book value per share (BVPS).

The dividend yield, expressed as a percentage, is a financial ratio (dividend/price) that shows how much a company pays out in dividends each year relative to its stock price.

Price/Earnings ratio (P/E) is an equity valuation multiple. It is defined as market price per share divided by annual earnings per share

USDCNY exchange rate refers to how many Renminbi one US dollar is worth.

Top Fund Holdings as of 9/30/2023:

1.	NetEase Inc	4.98%
2.	Shenzhen Inovance Technology Co Ltd	4.16%
3.	China Medical System Holdings Ltd	4.14%
4.	NARI Technology Co Ltd	4.03%
5.	Suofeiya Home Collection - A Shares	3.96%
6.	Zhejiang Supor Cookware - A Shares	3.74%
7.	TravelSky Technology Ltd	3.73%
8.	Haier Smart Home Co Ltd	3.69%
9.	Baidu Inc	3.66%
10.	Tencent Holdings Ltd	3.56%